No. 82-1869

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

MORRIS L. LEWY, et al.,

Petitioners,

—v.—

WILLIAM B. WEINBERGER, et al.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the Court of Appeals erred in its unanimous holding that the District Court did not abuse its discretion in approving a class action settlement when, with the benefit of extensive discovery conducted by plaintiffs and detailed findings and conclusions made after hearings by a Bankruptcy Court in related proceedings, the District Court found that the settlement was negotiated at arm's length by experienced counsel and was fair, adequate and reasonable.

PARTIES

The named petitioners are stated to be: Morris L. Lewy, Melvin Kimmel, Helen Sisk, Mildred B. Anderson, Gerald J. Anderson, Walter E. Barrie, Anne Crawford, Malcolm Pine, Herbert Lapham, Arthur Garson, Andre R. Jurkiewicz, Archie Plescia and Anne Plescia (Petition at 1-2).

Plaintiffs-respondents are: William B. Weinberger, Robert Smith, Stein Family Foundation, Inc., Edith Citron, Leo E. Panzirer, and Emanuel G. Rosenblatt.

Defendants-respondents are: Morgan Guaranty Trust Company of New York, Citibank, N.A., The Sanwa Bank, Ltd., The Chase Manhattan Bank, N.A., Chemical Bank, Manufacturers Hanover Trust Company, Irving Trust Company, Marine Midland Bank, Bankers Trust Company, The Bank of New York and DeWitt Peterkin, Jr. (Mr. Peterkin is a respondent only as to certain claims against him which were settled along with the claims against the bank defendants named in the complaint.)

This brief in opposition is submitted on behalf of defendants-respondents.*

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* Information provided in accordance with Rule 28.1 of the Supreme Court Rules may be found in the Appendix.

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OPINIONS BELOW

The opinion of the Court of Appeals (Waterman, Friendly and Meskill, *JJ.*), reported at 698 F.2d 61 (2d Cir. 1982) *sub nom. Weinberger v. Kendrick,* is set forth in the appendix to the petition at pages 1a-47a. The opinion of the District Court (Duffy, *J.*) bearing the same title is reported at 91 F.R.D. 494 (S.D.N.Y. 1981).

The Bankruptcy Court's opinion in the related case *In re W. T. Grant Co.,* upon which the courts below relied, is reported

at 4 B.R. 53 (Bankr. S.D.N.Y. 1980) (Galgay, *J.*), and its affirmance by the District Court (Duffy, *J.*) is reported at 20 B.R. 186 (S.D.N.Y. 1982). The affirmance of that decision by the Court of Appeals (Waterman, Friendly and Meskill, *JJ.*) is reported at 699 F.2d 599 (2d Cir. 1983), *petition for cert. filed,* ____ U.S.L.W. ____ (U.S. June 3, 1983) (No. 82-1985).

STATEMENT OF THE CASE

The opinion of Judge Friendly below sets forth the facts of this class action settlement of federal and state law securities claims against the lending banks of the now bankrupt W. T. Grant Company. 698 F.2d at 64-69. Factual errors in the petition as to the background of the settlement are not addressed here because of the accuracy and comprehensiveness of the opinion below and the unimportance of those errors to consideration of the petition. Certain points stressed by Judge Friendly deserve mention:

1. Following the filing of Grant's bankruptcy petition the bankruptcy trustee, "who commanded financial resources and professional assistance . . . not always available to plaintiffs' counsel in class actions," *id.* at 74, conducted "extensive investigations," including a "far-reaching and intensive probe of the banks' involvement in Grant's affairs during the class period." *Id.* at 66.

2. On the basis of such investigation the bankruptcy trustee and Bankruptcy Judge Galgay concluded that the chances of proving fraud or any other wrongdoing by the lending banks were "extremely slim" and "very remote," *id.* at 66, 75, and that the transactions between the banks and Grant had been "the result of arms-length negotiations conducted in good faith and governed by the dictates of sound business judgment." *Id.* at 75.

3. In the case at bar, plaintiffs' counsel "engaged in a wide range of discovery during the four years prior to the commencement of settlement discussions," *id.* at 67, and had

access to the "extensive and detailed" discovery of Grant's trustee, whose "discovery efforts were extremely relevant to the plaintiffs' claims." *Id.* at 74. Plaintiffs' discovery efforts were "substantially more thorough than those in many other decisions where settlements have been approved." *Id.*

4. "Like Grant's trustee and Judge Galgay, however, plaintiffs' counsel found virtually nothing to substantiate their allegations against the banks. . . ." *Id.* at 67.

5. All of the discovery materials, together with the "several careful and well-reasoned opinions by Bankruptcy Judge Galgay, . . . provided a satisfactory record on which the district court could base its decision." *Id.* at 74.

6. The court below found that plaintiffs would have faced "serious difficulties" establishing a fiduciary relationship between the lending banks and the Grant security holders and concluded:

> "Even assuming that the banks could be shown to stand in a fiduciary relation to Grant's security holders, the record indicates that neither they nor Peterkin, who as a director concededly was in such a relation, engaged in any wrong-doing." *Id.* at 79.

7. Petitioners' state court action (*Lewy*) "would require proof of fault identical to what would be demanded in the *Weinberger/Panzirer* cases [at bar]," *id.* at 70 n.12, and involved claims "generally less valuable" and more susceptible to "legal obstacles" than the federal claims—indeed, the state law claims were "extremely weak." *Id.* at 78-79.

8. The court below found that the appropriateness of settlement in the federal court was clear since "[t]he exclusivity of federal jurisdiction over claims for violation of the Securities Exchange Act makes a federal court the only one where a complete disposition of federal and related state claims can be rendered." *Id.* at 76.

9. Petitioners "had complete access to the extensive materials" compiled in the litigations; they "appear to have done little to explore" those materials or take discovery in their state court action (*Lewy*); they "came forward with no specific objections to the substantive fairness of the settlement"; and "they have provided no specific criticisms of Judge Galgay's careful examination of the relationship between the banks and Grant." *Id.* at 79.

REASONS FOR DENYING CERTIORARI

There are no special and important reasons of the character described in the Court's Rule 17 for review on writ of certiorari. The Points raised in the petition will be discussed in order, except for Point Seven as to which there is no disagreement.

1. Class Certification May Coincide with Settlement

In Point One petitioners contend that, by permitting class certification to be postponed until the settlement agreement had been filed with the district court, the Second Circuit violated Federal Rule of Civil Procedure 23 and diverged from the decision of the Seventh Circuit in *In re General Motors Corp. Engine Interchange Litigation,* 594 F.2d 1106 (7th Cir.), *cert. denied sub nom. Oswald v. General Motors Corp.,* 444 U.S. 870 (1979) (Petition at 9-11).

The decision below is consistent with the decisions of other Circuits that the postponement of class certification until filing of a class settlement is permissible under Rule 23. *See, e.g., In re Corrugated Container Antitrust Litigation,* 643 F.2d 195, 223 (5th Cir. 1981); *In re Beef Antitrust Litigation,* 607 F.2d 167, 173-78 (5th Cir. 1979), *cert. denied sub nom. Iowa Beef Processors, Inc. v. Meat Price Investigators Ass'n,* 452 U.S. 905 (1981); *Marshall v. Holiday Magic, Inc.,* 550 F.2d 1173, 1176 (9th Cir. 1977); *Ace Heating & Plumbing Co. v. Crane Co.,* 453 F.2d 30, 33-34 (3rd Cir. 1971). Judge Friendly's opinion fully explains the refusal of courts to prohibit this common practice, noting in particular the great flexibility in

class action management conferred upon the district courts by Rule 23 and the proven utility of stipulated settlement classes in resolving class actions. 698 F.2d at 72-73.

The decision below also conforms to the holding of *General Motors*. The court below examined the negotiation process leading to the settlement and saw "nothing" in petitioners' argument that the district court failed to scrutinize that process closely:

> "The district court noted the absence of any indication of collusion, the protracted settlement negotiations, the ability and experience of plaintiffs' counsel, the extensive discovery preceding settlement and the fact that counsel for all parties—including the objectors—had access to materials produced in discovery, including the extensive and detailed discovery of Grant's trustee, who commanded financial resources and professional assistance . . . not always available to plaintiffs' counsel in class actions. All these considerations, as previous decisions have noted, . . . are important indicia of the propriety of settlement negotiations. Indeed, . . . plaintiffs' presettlement preparation and discovery efforts in this case were substantially more thorough than those in many other decisions where settlements have been approved." *Id.* at 74 (citations omitted).

Compare General Motors, 594 F.2d at 1123-33. The Second Circuit also satisfied itself that the settlement treated state law claimants fairly and adequately since (i) all had the right to opt out and could make that decision with full knowledge of the terms of the settlement, 698 F.2d at 72, (ii) those who did opt out retained the right to proceed with state court litigation and were informed of this right in the notice of settlement, *see id.* at 70, (iii) none was dismissed without compensation, as had occurred prior to the Seventh Circuit's reversal of the district court in *General Motors,* and (iv) those who accepted the settlement received compensation found to be adequate. *Id.* at 78-79. *Compare General Motors,* 594 F.2d at 1133-37. In fact, the Second Circuit expressly affirmed the correctness of

General Motors and disavowed any intention to depart from it. 698 F.2d at 81-82.

2. The Settlement Is Not Unfair to State Law Claimants

Point Two of the petition makes various allegations in an apparent effort to show that the settlement is somehow unfair to state law claimants (Petition at 11-13).

First, the settlement is said to be "collusive", a point explicitly rejected by both courts below. *See* 698 F.2d at 74.

Second, the consolidated complaint below is said to have "copied" the state law claims in *Lewy* when, in fact, the original complaint below, which preceded the *Lewy* complaint, alleged state law claims of purchasers of Grant securities from the beginning. *Id.* at 64.

Third, the parties to the settlement are accused of failing to conduct any proceedings with respect to state law claims. The court below found, however, that discovery which was "far-reaching and intensive" formed the basis for the settlement in this case, *id.* at 66, whereas counsel for petitioners conducted almost no discovery in *Lewy*. *Id.* at 72, 79.

Fourth, the state law claimants who did not opt out of the settlement are said to have been greatly undercompensated in comparison with settling debentureholders in *In re W. T. Grant Co.*, a contention answered in Point 4 below.

Fifth, petitioners assert that "the settlement in this case, in effect, gives the debenture holders nothing because the settlement received in the Bankruptcy Proceeding is *deducted* from the settlement received in this case" (Petition at 12). That is incorrect. Both settlements contain set-off provisions designed to prevent double recovery by any present holders of debentures who also belong to one of the plaintiff classes in the case at bar.

Sixth, the district court is said to have violated the "salutory doctrine" that "a Court that first has jurisdiction of a controversy is entitled to proceed to a conclusion . . ." (Petition

at 13). In fact, *Weinberger* was the first class action securities complaint arising out of the demise of Grant, the district court never enjoined the later state court proceedings in *Lewy,* and the lack of progress in those proceedings stemmed entirely from a failure to prosecute that action. *See* 698 F.2d at 79.

3. Voluntary Inclusion in a Settlement of Pendent State Law Claims Is Appropriate

In Point Three petitioners challenge the inclusion in the settlement class of those who may have state law claims based solely on the holding of Grant securities. Petitioners argue that *Blue Chip Stamps v. Manor Drug Stores,* 421 U.S. 723 (1975), and *National Super Spuds v. New York Mercantile Exchange,* 660 F.2d 9 (2d Cir. 1981), prohibit the exercise of pendent jurisdiction over such state law claims (Petition at 13-15).

Neither decision supports petitioners' argument. *Blue Chip* held that mere holders of securities have no cause of action under the federal securities laws, but did not treat the subject of pendent jurisdiction over the state law claims of such holders, and certainly not in the context of a settlement. The Second Circuit's decision in *National Super Spuds* is also inapplicable, as explained below by Judge Friendly, who also authored *National Super Spuds:*

> "In [*National Super Spuds*] class certification had been ordered fairly early in the game . . . . The settlement, executed a year after notice of the certification had been sent and long after the opting out period expired, purported to settle claims going beyond those asserted on behalf of this class . . . ."
>
> "The situation here is quite different. Before the class was certified, it was expanded to include persons holding state as well as federal claims. The notice sent to security holders clearly stated this and afforded an opportunity to opt out. Moreover, the settlement made provision for payments to holders of state claims although these were generally less than to holders of federal claims. We have no intention to depart in any way from *National Super*

> *Spuds*; we simply find it inapplicable to the facts here and hold, in agreement with other courts, that there is no rigid rule against the addition of new claims shortly before submission of a proposed settlement provided that proper notice and opportunity for opting out are afforded . . . and that the settlement fairly and adequately provides for the new claims." 698 F.2d at 77 (citations omitted).

The Second Circuit found that "[t]he circumstances here are about as powerful for the exercise of pendent party jurisdiction as can be imagined." *Id.* at 76. Judge Friendly outlined five reasons for approving "the joinder of plaintiffs in a *settlement* of an action involving Rule 10b-5 and state law claims," *id.* at 77 n. 15:

(i) The exclusive jurisdiction of the federal courts over claims brought under the Securities Exchange Act rendered the federal court "the only one where a complete disposition of federal and related state claims can be rendered." *Id.* at 76.

(ii) Contrary to the concern most frequently voiced concerning pendent party jurisdiction, exercise of such jurisdiction in this case did not "[require] a party not otherwise subject to suit in federal court to defend himself in that forum. . . . In this case pendent party jurisdiction serves . . . to extend federal jurisdiction to a new group of *plaintiffs*." *Id.* at 77 (citations omitted) (emphasis in original).

(iii) Any plaintiff who did not wish to settle in the federal court had the right to opt out of the settlement and pursue his claims in state court. *Id.*

(iv) The same state law claims were "already before the federal courts," having been asserted by persons with federal claims, so the federal court would have to resolve the state law claims in any event. *Id.* at 76-77.

(v) In this case "extension of pendent party jurisdiction permits the comprehensive settlement of plaintiffs' claims, thus furthering the policies underlying *Blue Chip Stamps*." *Id.* at 77 n. 15.

4. The Settlement Amount Is Neither Inadequate Nor a Ground for Certiorari

The amount paid in settlement is not an appropriate ground for certiorari. In *City of Detroit v. Grinnell Corp.*, 495 F.2d 448, 455 (2d Cir. 1974), Judge Moore observed that the "fact that a proposed settlement may only amount to a fraction of the potential recovery does not, in and of itself, mean that the proposed settlement is grossly inadequate and should be disapproved." The court below found the state law claims to be weak and the settlement to be fair on a record showing that neither the lending banks nor Peterkin "engaged in any wrongdoing." 698 F.2d at 79. The Bankruptcy Court settlement was larger because it involved contract claims directly against the Grant estate of individuals still holding Grant subordinated debentures, not equity holders as here or debentureholders who have already recovered through sale of their bonds in the market. While the main underlying facts in issue are the same, the priorities of recovery in a bankruptcy context necessarily differ. *See In re Stirling Homex Corp.*, 579 F.2d 206 (2d Cir. 1978), *cert. denied sub nom. Jezarian v. Raichle*, 439 U.S. 1074 (1979).

5. Reliance by the Courts Below on the Related Bankruptcy Court Decisions Was Appropriate

In analyzing the settlement the courts below relied on the "wide range of discovery" taken by plaintiffs' counsel, 698 F.2d at 67, together with "the materials amassed in the [bankruptcy] trustee's investigation," *id.* at 74, and also the "careful and well-reasoned opinions by Bankruptcy Judge Galgay." *Id.* The appropriateness of reliance on Judge Galgay's opinions was made clear by Judge Friendly:

> "Since [the trustee's] claim of equitable subordination required a detailed inquiry into the relationship between the banks and Grant, which is precisely the issue raised in the *Weinberger/Panzirer* actions, his discovery efforts were extremely relevant to the plaintiffs' claims."

* * *

> "Central to plaintiffs' claims against the banks under both the federal securities laws and the common law was the allegation that the defendants 'were in a position to, and did, control, influence and participate in Grant's operations.' Consolidated Amended Complaint ¶ 28. This precise point had been considered by Judge Galgay in Grant's bankruptcy proceedings."
>
> * * *
>
> "Indeed, as the . . . findings of Judge Galgay on the closely-related subject of equitable subordination show, . . . there is virtually no evidence that the defendants engaged in any wrongdoing in their dealings with Grant." 698 F.2d at 74-75, 79.

Not only were the facts and proof largely the same, but the same district and circuit judges who reviewed the settlement at bar also reviewed Judge Galgay's decision. In fact, the Second Circuit stayed its mandate in the case at bar until it had an opportunity to review the appeal from Judge Galgay's decision. *Id.* at 81.

6. The Anti-Injunction Act Is Inapplicable

Petitioners argue that the Anti-Injunction Act, 28 U.S.C. § 2283, prohibits approval of the settlement because "the federal court has, as a practical matter, enjoined a State Proceeding and prevented the prosecution of State Claims in the forum where they were initially presented" (Petition at 22).

The Anti-Injunction Act is inapplicable to this case because the district court never enjoined state court proceedings. On the contrary, the *Lewy* plaintiffs (petitioners here) sought to enjoin the federal court and requested the state court to certify a competing class. The state court declined, *Lewy v. Chase Manhattan Bank, N.A.*, N.Y.L.J., Jan. 8, 1981, at 6, cols. 3, 4-6 (N.Y. Sup. Ct. 1981):

> "While the Federal Court might not have had jurisdiction over these 'state action' claims if they were the only ones brought before it, clearly under the doctrine of

pendent jurisdiction those claims are properly before it, and it is obvious that the order granting the amendment was within the power and the discretion of the Federal Court."

* * *

"It is clear from the nature of the claims that concentration of the litigation in one forum is desirable, not only from the point of view of judicial economy, but to reduce the expenses of litigation . . . ."

"Although plaintiffs would like to create a jurisdictional contest between the two courts, by giving these plaintiffs the right to act on behalf of class members in the class created by the Federal Court by opting out, thereby undermining the jurisdiction and orders of the District Court, . . . [t]his court would be abusing its discretion if it gave such power in this case. Neither will this court enjoin the defendants, as plaintiffs request, from defending their interests in the Federal Court in any way, whether by trial or settlement or otherwise . . . . This court is loath to enter such a race."

CONCLUSION

For the reasons set forth above, the petition for a writ of certiorari should be denied.

Dated: New York, New York
June 16, 1983

Respectfully submitted,

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APPENDIX

Pursuant to Rule 28.1 of the Rules of the Supreme Court, defendants-respondents provide the following list of settling corporate parties and further information about the agent and lead bank for this group, Morgan Guaranty Trust Company of New York ("Morgan Guaranty").

Morgan Guaranty is a wholly owned subsidiary of J.P. Morgan & Co. Incorporated. Morgan Guaranty's subsidiaries (except wholly owned subsidiaries) are: Banco Morgan Finansa and Bank Morgan Labouchere N.V. Eleven subsidiaries are wholly owned by Bank Morgan Labouchere N.V. Morgan Guaranty has no affiliates other than those wholly owned by its parent, J.P. Morgan & Co. Incorporated, or by one of its parent's wholly owned subsidiaries.

Corporate respondents named as defendants in the action below, in addition to Morgan Guaranty, are Citibank, N.A., The Sanwa Bank, Ltd., The Chase Manhattan Bank, N.A., Chemical Bank, Irving Trust Company, Manufacturers Hanover Trust Company, Marine Midland Bank, Bankers Trust Company and The Bank of New York.

The settlement also extends to the following additional banks, for which Morgan Guaranty acted as agent in connection with the loans to W. T. Grant Company: Bank of America National Trust & Savings Association, Connecticut Bank and Trust Company, Continental Illinois National Bank and Trust Company of Chicago, Equibank, N.A., The First National Bank of Atlanta, First American National Bank, First National State Bank of New Jersey, Flagship First National Bank of Miami, Manufacturers & Traders Trust Company, Mellon Bank, N.A., Seattle-First National Bank, Security Pacific National Bank, United American Bank (now First Tennessee Bank), United California Bank, Wells Fargo Bank, N.A. and Wilmington Trust Company.

Should the Court desire additional disclosure with respect to any of the above, such information will be provided promptly.